GSC, Engle, Telco and the Reliable Trust owned 42,800 shares of OSI, or approximately 2.98% of the outstanding shares. Telco and later Telvest continued to purchase OSI stock steadily until March 1979, when the group's holdings were 312,400 shares, or 21.73% of outstanding shares. On May 3, 1978, Engle and Newbill visited OSI management and asked that Engle be put on the OSI board, but the proposal was rejected. A few days later, Telco and Libco filed with the Securities and Exchange Commission a Schedule 13D revealing the Engle group's purchases of OSI stock and their intentions to acquire more shares. The Schedule 13D said "Libco may be deemed to own beneficially an additional 12,500 shares of OSI owned of record by the Reliable Manufacturing Corporation Employees Profit Sharing Trust ('Reliable Trust')," and it stated that Libco could elect the directors of Reliable who in turn appointed the Reliable Trust administrators. The statement also noted that Zuckerman was a director of both Libco and Reliable, president of Reliable and one of the Reliable Trust administrators. In the Schedule 13D, Libco expressly disclaimed "any beneficial interest in the assets of the Reliable Trust." [FN13]

FN13. Neither the mention of the trust's shares nor the disclaimer is conclusive regarding the use of the trust's assets. However, the filing is clear evidence that Libco, Telco and Engle (who signed the filing for Telco) knew of the trust's investments in OSI. *See supra* note 11.

In early 1979 the Engle group battled OSI management for control of the company through two tender offers and a proxy fight. Documents filed in the tender offers continued to show the relationship between the Reliable Trust and other group members. Dardick acted as attorney for Telco in the tender offers and for Telvest in the proxy fight. During the proxy fight, Dardick ordered the Harris Bank as trustee to vote the trust's shares in favor of the Telvest slate of directors on April 24, 1979. During these struggles, Dardick was sharply critical of OSI management and the company's profitability. At the same time, Dardick controlled the Reliable Trust's investments in OSI, and his statements indicate that he believed the investments could have turned out well only if OSI management could have been replaced, or if the ***121** trust could have sold its shares to a "white knight" for a premium.

By May 1979, the Engle group controlled 21.73% of OSI shares. The control contest ended when the Brown Group, Inc., entered as a "white knight" on behalf of OSI management and tendered $15.00 per share of OSI stock. On June 26, 1979, the Reliable Trust sold its OSI shares to the Brown Group for a profit of 141%.

3. *Hickory Furniture investments:* Hickory was the third investment target, and the Engle group succeeded in purchasing a majority of Hickory stock by October 1979. The Reliable Trust bought 8000 shares of Hickory on March 22, 1978. At that time, Libco and GSC already owned 50,400 shares, and the trust purchases gave the group 4.88% of outstanding Hickory stock. After the April 21st Telco meeting, Telco and later Telvest steadily acquired Hickory stock.[FN14] The Reliable Trust purchased an additional 4000 shares of Hickory on June 9, 1978. Hickory management did not resist the Engle group investments, and on June 28th, Engle became a member of the Hickory board of directors. By the end of 1978, the Engle group owned 32.8% of Hickory, and their holdings grew to 52.8% in October 1979. The Reliable Trust sold its 12,000 shares of Hickory on March 19, 1979, one year after its initial purchase, for a net profit of 4%.

FN14. Libco and Telco filed a Schedule 13D with the Securities and Exchange Commission in May 1978 regarding their purchases of Hickory stock. Later filings to update the original Schedule 13D describe the Reliable Trust's holdings of Hickory stock and say that "Libco may be deemed to own beneficially" the trust's shares. Libco also disclaimed "any beneficial interest in the assets of the Reliable Trust." Again, the statements in the SEC filings are not conclusive as to whether the Engle group used the Reliable Trust's assets in its acquisition program. *See supra* notes 11 and 13. Nevertheless, the filings clearly show that Telco, Libco and Engle were aware of the Reliable Trust's Hickory investments.

C.

The case before us was tried in the district court before Judge Leighton in September 1982. The district court granted judgment for defendants in an unpublished memorandum issued November 18, 1982. The district court held first that ERISA does not create a cause of action where the plan does not suffer financial loss. Conclusion of Law No. 10. The district court also found that the defendants did not use the Reliable Trust assets for their own purposes and that the assets were used exclusively in the interest of the trust beneficiaries.

Findings of Fact Nos. 11, 12, 13 and 18; Conclusions of Law Nos. 4 and 15. The district court held that Dardick, Zuckerman and the National Boulevard Bank were fiduciaries of the trust, but that they had not violated their duties under ERISA sections 404 and 406, 29 U.S.C. §§ 1104 and 1106, by investing the trust assets in Berkeley, OSI and Hickory. Conclusions of Law Nos. 2, 4, 5, 6 and 15. The court concluded that the plan assets had been used for the exclusive benefit of the plan beneficiaries, Conclusion of Law No. 15, and that the plan administrators acted in good faith, Finding of Fact No. 23. The court also concluded that Dardick, Zuckerman and the National Boulevard Bank did not breach their co-fiduciary obligations under 29 U.S.C. § 1105(a). The court held further that Engle, Libco, Telco and Telvest had not exercised discretionary authority over the Reliable Trust and were not fiduciaries with respect to the investment or administration of its assets. Findings of Fact Nos. 21 and 22; Conclusion of Law No. 7. The court awarded expenses and attorneys' fees to all defendants and held that Dardick, Zuckerman and the National Boulevard Bank were entitled to reimbursement of expenses and fees from the trust's remaining assets. Conclusion of Law No. 16.

II.

[1] The Reliable Trust's investments in Berkeley, OSI and Hickory produced in the aggregate the extraordinary return on investment of 72%, exclusive of dividends.[FN15] It is clear that the trust lost no money in ***122** the challenged transactions. The district court held that ERISA creates no cause of action where a breach of fiduciary duty does not cause financial harm to the benefit plan, Conclusion of Law No. 10, but the district court erred in this statement of the law. ERISA clearly contemplates actions against fiduciaries who profit by using trust assets, even where the plan beneficiaries do not suffer direct financial loss.[FN16] A fiduciary who breaches his duties "shall be personally liable ... to restore to such plan any profits of such fiduciary which have been made through use of assets of the plan by the fiduciary." 29 U.S.C. § 1109(a).

FN15. See *supra* note 9.

FN16. The district court's reliance on *Alton Memorial Hospital v. Metropolitan Life Ins. Co.*, 656 F.2d 245, 249 (7th Cir.1981), is misplaced. That case involved a contractual dispute between an employer who maintained a pension plan and the enrolled actuary of the plan. This court there held that the actuary could not invoke ERISA's fiduciary standards to recover from the employer in the contractual dispute between them. It was clear that the interests of the plan beneficiaries were not affected in any way, and thus ERISA did not create a cause of action on behalf of the actuary. In the present case, by contrast, the interests of plan beneficiaries were directly affected. The defendants appear to have risked the trust assets in part to serve their own purposes rather than solely the interests of the beneficiaries. With its focus on protecting the interests of plan beneficiaries, ERISA clearly prohibits such actions, and the provisions in section 1109(a) for disgorgement of profits are the remedy to deter such violations.

The nature of the breach of fiduciary duty alleged here is not the *loss* of plan assets but instead the *risking* of the trust's assets at least in part to aid the defendants in their acquisition program. ERISA expressly prohibits the use of assets for purposes other than the best interests of the beneficiaries, and the language of section 1109(a) providing for disgorgement of profits from improper use of trust assets is the appropriate remedy.[FN17] On the record before us, we are unable to determine the extent of the defendants' total profits, and we certainly cannot measure the extent, if any, to which any profits resulted from the defendants' use of the trust assets. However, those questions are relevant only in measuring damages. *See infra* Part VI. At this point in the analysis, we need only say that plaintiffs are not required to show that the trust lost money as a result of the alleged breaches of fiduciary duties. If ERISA fiduciaries breach their duties by risking trust assets for their own purposes, beneficiaries may recover the fiduciaries' profits made by misuse of the plan's assets.

FN17. The legislative history of ERISA shows that Congress intended disgorgement of profits to be one remedy available for breach of fiduciary duty. A fiduciary who breaches this duty "must restore to the plan any profits which he made using plan assets." S.REP. NO. 383, 93rd Cong., 1st Sess. 105, *reprinted in*1974 U.S.CODE CONG. & AD.NEWS 4890, 4988. The disgorgement provisions of § 1109(a) are in accord with the common law of trusts. *See*RESTATEMENT (SECOND) OF TRUSTS § 205(b), comment (h), and § 206 comment (j)

(1959). *See also* *Home Federal Savings & Loan Ass'n v. Zarkin*, 89 Ill.2d 232, 59 Ill.Dec. 897, 432 N.E.2d 841, 848 (1982). The purpose of this strict rule is to deter breaches by denying fiduciaries any profits from their misuse of assets. G. BOGERT, THE LAW OF TRUSTS AND TRUSTEES § 543 at 218 (rev. 2d ed. 1978).

III.

ERISA requires those who control employee benefit plans to act solely in the interests of the plan beneficiaries. The fiduciary duties of those who control benefit plans are set forth in part 4 of Title I of ERISA. Two sections are applicable to this case. First, section 404(a), 29 U.S.C. § 1104(a), codifies and makes applicable to fiduciaries [FN18] certain principles developed in ***123** the law of trusts.[FN19] H.R.Rep. No. 533, 93rd Cong., 1st Sess. 11, 13, *reprinted in*1974 U.S. Code Cong. & Ad. News 4639, 4649, 4651. Section 404(a)(1) provides in relevant part that:

FN18. "Fiduciary" is defined in ERISA as follows:

(A) Except as otherwise provided in subparagraph (B), a person is a fiduciary with respect to a plan to the extent (i) he exercises any discretionary authority or discretionary control respecting management of such plan or exercises any authority or control respecting management or disposition of its assets, (ii) he renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so, or (iii) he has any discretionary authority or discretionary responsibility in the administration of such plan. Such term includes any person designated under section 1105(c)(1)(B) of this title.

29 U.S.C. § 1002(21)(A). We discuss below the application of this definition to the defendants in this case.

FN19. As one district court has stated:

The legislative history of the [fiduciary duty] sections of ERISA indicates, that to the extent practical, the obligations of trustees of pension funds and the limitations on their power of investment were to be interpreted under principles applicable to trustees under the common law of trusts, with a view toward establishing uniform standards.

Marshall v. Teamsters Local 282 Pension Trust Fund, 458 F.Supp. 986, 990 (E.D.N.Y.1978) (fn. omitted).

a fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and-

(A) for the exclusive purpose of:

(i) providing benefits to participants and their beneficiaries; and

(ii) defraying reasonable expenses of administering the plan;

(B) with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims ....

29 U.S.C. § 1104(a)(1). For the case before us, the key provisions are those requiring the fiduciary to act "solely in the interest" of plan beneficiaries and for "the exclusive purpose" of providing benefits. Other federal courts have described the duty of loyalty under ERISA as the duty to act with "complete and undivided loyalty to the beneficiaries of the trust,"*Freund v. Marshall & Ilsley Bank*, 485 F.Supp. 629, 639 (W.D.Wis.1979), and with an "eye single to the interests of the participants and beneficiaries,"*Donovan v. Bierwirth*, 680 F.2d 263, 271 (2d Cir.), *cert. denied*,459 U.S. 1069, 103 S.Ct. 488, 74 L.Ed.2d 631 (1982).

Second, section 406 of ERISA, 29 U.S.C. § 1106, prohibits transactions in which the potential for misuse of plan assets is particularly great. The prohibited transaction rules focus primarily on the relationship between the benefit plan and other parties to a transaction, and the section prohibits transactions where those dealing with the plan may have conflicting interests which could lead to self-dealing. For example, section 406(a)(1)(B) prohibits loans between benefit plans and parties in interest. The *per se* rules of section 406 make much simpler the enforcement of ERISA's more general fiduciary obligations. *See*S.REP. NO. 383, 93rd Cong., 1st Sess. 95, *reprinted in*1974 U.S.CODE CONG. & AD.NEWS 4890, 4979.

Section 406 also includes broader language which may require a more detailed analysis of the fiduciary's actions. The provisions relevant to this case are:

(a) Except as provided in section 1108 of this title:

(1) A fiduciary with respect to a plan shall not cause the plan to engage in a transaction, if he knows or should know that such transaction constitutes a direct or indirect-

(D) transfer to, or use by or for the benefit of, a party in interest, of any assets of the plan....

(b) A fiduciary with respect to a plan shall not-
(1) deal with the assets of the plan in his own interest or for his own account ....

29 U.S.C. § 1106. The relevant language here is quite broad: "use by or for the benefit of, a party in interest," § 1106(a)(1)(D),[FN20] and "deal ... in his own interest," § 1106(b)(1).

> FN20. ERISA defines "party in interest" at 29 U.S.C. § 1002(14). The definition includes Reliable Manufacturing, Libco, Telco, Telvest, Engle, Zuckerman, Dardick and the National Boulevard Bank. 29 U.S.C. § 1002(14)(A), (B), (C), (E), (G) and (H).

The district court found that Dardick and Zuckerman did not breach their fiduciary duties under ERISA by purchasing and holding stock in Berkeley, OSI and Hickory. The court found that the purchases were made upon the advice of Newbill and were ***124** intended to diversify the plan's investments. The court also held that it was not improper for the Reliable Trust to hold its stock in Berkeley, OSI and Hickory after Telco made major purchases of the stocks. The court concluded that the trust's investments were prudent and made exclusively for the benefit of the trust beneficiaries. The court also found that the purchases were not prohibited transactions under section 406. The district court therefore concluded that Dardick and Zuckerman did not breach their fiduciary duties under section 404 and section 406.

[2][3] We must accept the district court's findings of fact unless we find them "clearly erroneous." FED.R.CIV.P. 52(a); *Clark v. Universal Builders, Inc.*, 706 F.2d 204, 206 (7th Cir.1983). In this case, however, many of the district court's most important "Findings of Fact" regarding the use of the trust's assets are mixed findings of fact and law. *See* Findings of Fact Nos. 11, 12, 13, 17, 18, 19, 21, 22. Our review of these findings is consequently less deferential than it might otherwise be. *Harrison v. Indiana Auto Shredders Co.*, 528 F.2d 1107, 1120 (7th Cir.1975). *See Lektro-Vend Corp. v. Vendo Co.*, 660 F.2d 255, 262-63 (7th Cir.1981) (review of mixed findings and "paper" cases), *cert. denied*, 455 U.S. 921, 102 S.Ct. 1277, 71 L.Ed.2d 461 (1982). Further, the evidence relevant to our conclusions on the critical issues in this case consists of documents and undisputed oral testimony. The district court's findings on issues where the observation of witnesses is critical are, of course, fully subject to the clearly erroneous rule. However, the district court's findings as to the defendants' credibility and good faith are not relevant to our disposition of this case, and thus we do not decide whether they were clearly erroneous. *See* Finding of Fact No. 23. This litigation concerns the legal significance of undisputed facts-the disputed issues of credibility and subjective good faith simply do not come into play. Good faith is not a defense to an ERISA fiduciary's breach of the duty of loyalty. *See Donovan v. Bierwirth*, 538 F.Supp. 463, 470 (E.D.N.Y.1981), *aff'd as modified*, 680 F.2d 263 (2d Cir.), *cert. denied*, 459 U.S. 1069, 103 S.Ct. 488, 74 L.Ed.2d 631 (1982).

[4] In our view, application of ERISA's fiduciary standards to the Reliable Trust's investments in the corporate control contests here requires us to reverse the judgment below. The undisputed facts in the record show that the district court clearly erred when it concluded that plan assets were used exclusively in the interests of beneficiaries. The Reliable Trust administrators did not act solely in the interests of the plan beneficiaries where they invested the trust's assets in companies involved in corporate control contests, where the administrators themselves were actively engaged in the control contests and had substantial interests in them, where the administrators failed to make an intensive and independent investigation of the investment options open to the trust and where the trust's investment decisions never deviated from the best interests of the Engle group.

A. *Fiduciary Standards of Section 404.* The Second Circuit applied the fiduciary standards of section 404 to fiduciaries' conduct in a contest for corporate control in *Donovan v. Bierwirth*, 680 F.2d 263 (2d Cir.), *cert. denied*, 459 U.S. 1069, 103 S.Ct. 488, 74 L.Ed.2d 631 (1982). At issue were the actions of Grumman Corporation's pension fund trustees during the Grumman-LTV takeover battle. The trustees were also Grumman officers. The district court had stated that Grumman corporate insiders with fiduciary duties to the corporation's pension fund would be tested against a standard requiring them to undertake a vigorous and independent investigation into the wisdom of the contemplated investment in order to meet the section 404(a)(1)(B) standards:

[their] independent investigation into the basis for an investment decision which presents a potential conflict of

interests must be both intensive and scrupulous and must be discharged with the greatest degree of care that could be expected under all the circumstances by reasonable beneficiaries and participants of the plan.

125Donovan v. Bierwirth,* 538 F.Supp. 463, 470 (E.D.N.Y.1981), *aff'd as modified,* 680 F.2d 263 (2d Cir.), *cert. denied,* 459 U.S. 1069, 103 S.Ct. 488, 74 L.Ed.2d 631 (1982).

Writing for the Second Circuit on appeal, Judge Friendly considered two approaches to analyzing the trustees' duty of loyalty in managing plan assets during the takeover battle. The first approach focused on the existence of conflicting interests between the trustees and the plan beneficiaries. The pension trustees were obliged to make their decisions, Judge Friendly wrote, "with an eye single to the interests of the participants and beneficiaries." 680 F.2d at 271. That duty of loyalty imposed upon the trustees a duty "to avoid placing themselves in a position where their acts as officers and directors of the corporation will prevent their functioning with the complete loyalty to participants demanded of them as trustees of a pension plan." *Id.*[FN21] Where the plan trustees were officers of the takeover target, and where they clearly had substantial career and financial interests in the outcome of the control contest, the court said it believed it would have been "almost impossible" for the trustees to have decided to use the trust assets in ways which would weaken their own position in the control contest, regardless of the interests of the plan beneficiaries. 680 F.2d at 272. Thus, the first approach the Second Circuit considered would require fiduciaries who face substantial conflicts of interest in corporate control contests to step aside so that a neutral trustee could act for the duration of the control contest. The court approved of this approach, 680 F.2d at 271-72, but chose to rest its decision instead on the second approach which examined in great detail the trustees' investigation of the alternatives open to them. The court held that the trustees' investigations did not amount to the thorough, careful and impartial investigation needed to justify actions which would, at least incidentally, benefit themselves and their corporation, apart from their effects on the beneficiaries of the trust:

> FN21. We recognize, as did the court in *Donovan v. Bierwirth,* that ERISA contains express exceptions which permit fiduciaries to act in a few limited situations where their interests and those of plan beneficiaries may diverge. *See* 29 U.S.C. § 1108. However, the exceptions of section 1108 are quite limited, and abuses are reasonably easy to detect where, for example, a trustee pays himself an excessive salary. None of the exceptions in section 1108 is applicable here.

they should have realized that, since their judgment on this score could scarcely be unbiased, *at the least they were bound to take every feasible precaution to see that they had carefully considered the other side,* to free themselves, if indeed this was humanly possible, from any taint of the quick negative reaction characteristic of targets of hostile tender offers ..., and particularly to consider the huge risks attendant on purchasing additional Grumman shares at a price substantially elevated by the tender offer.

680 F.2d at 276 (emphasis supplied).

Under the section 404(a) duty of loyalty, the central question is whether the fiduciaries acted solely in the interests of the beneficiaries and for the exclusive purpose of providing them with benefits. The two approaches considered in *Donovan v. Bierwirth* offer two avenues for dealing with this central question. The first avenue focuses on the potential for conflicts of interest between the fiduciaries and the plan beneficiaries. Where the potential for conflicts is substantial, it may be virtually impossible for fiduciaries to discharge their duties with an "eye single" to the interests of the beneficiaries, and the fiduciaries may need to step aside, at least temporarily, from the management of assets where they face potentially conflicting interests. The second avenue involves a broader inquiry into the fiduciaries' actions where they may have substantial interests in a control contest. In *Donovan v. Bierwirth,* the Second Circuit focused on the fiduciaries' actions in investigating the investment options open to the plan during the corporate control contest. Where it might be possible to question the fiduciaries' loyalty, they are obliged at a minimum to engage in an intensive***126** and scrupulous independent investigation of their options to insure that they act in the best interests of the plan beneficiaries. 538 F.Supp. at 470; 680 F.2d at 272. In the case before us, we believe there is an additional factor which weighs heavily in evaluating the loyalty of the fiduciaries. Here the control efforts lasted for several months, and in the case of Hickory, for over a year. The Reliable Trust held its shares involved in the control contests throughout these periods, and, as we discuss below, the trust's use of its assets at all relevant times tracked the best interests of the

Engle group in the control contest. We believe that the extent and duration of these actions congruent with the interests of another party are also relevant for courts in deciding whether plan fiduciaries were acting solely in the interests of plan beneficiaries.

[5] B. *Prohibited Transactions Under Section 406.* Before discussing the application of the fiduciary standards to this case, we must also examine the applicability of the prohibited transaction provisions of section 406. In *Donovan v. Bierwirth,* the Second Circuit declined to apply the prohibited transaction provisions of section 406 to that case involving the use of an employee pension plan's assets to defend the employer from a hostile tender offer. 680 F.2d at 270. Specifically, the court there refused to apply the provisions of section 406(b)(2) prohibiting a fiduciary from acting on behalf of a party with interests adverse to the plan or its participants and beneficiaries. The Second Circuit stated that subsection (b)(2) was the only "arguably applicable" provision in section 406. The court said:

> We see no reason to think Congress intended the expansive interpretation of the various specific prohibitions of § 406 urged by the Secretary, particularly in light of the inclusion of the sweeping requirements of prudence and loyalty contained in § 404.
>
> 680 F.2d at 270.

However, we believe that the protective provisions of section 406(a)(1)(D) and (b)(1) should be read broadly in light of Congress' concern with the welfare of plan beneficiaries. We read those provisions dealing with the use of plan assets for the benefit of "parties in interest" and plan fiduciaries as a gloss on the duty of loyalty required by section 404.

We do not believe that Congress intended the language "use by or for the benefit of, a party in interest," § 406(a)(1)(D), and "deal ... in his own interest," § 406(b)(1), to be interpreted narrowly. The entire statutory scheme of ERISA demonstrates Congress' overriding concern with the protection of plan beneficiaries, and we would be reluctant to construe narrowly any protective provisions of the Act.

The broad provisions of section 406(a)(1)(D) and (b)(1) require courts to look carefully at the transaction to decide whether plan assets were used "by or for the benefit of" a party in interest, or whether a fiduciary dealt with the plan assets "in his own interest." Application of these provisions may require courts to engage in the same searching investigation into the objective circumstances of the fiduciary's actions needed to apply the fiduciary loyalty provisions of section 404(a)(1).

[6] Section 406(a)(1)(D) should be read to cover the actions of a trustee who buys shares in a target corporation in order to assist either the target's management or the raider in its quest for corporate control or a "control premium." If the corporation which the fiduciary seeks to aid qualifies as a "party in interest," we see nothing in the language or legislative history of subsection (a)(1)(D) which would preclude a court from treating the purchase as the use of plan assets for the benefit of a party in interest, at least where other evidence shows the fiduciary's purpose. *See Dimond v. Retirement Plan,* 582 F.Supp. 892, 4EMPLOYEE BEN.CAS. (BNA) 1457, 1463 (W.D.Pa. 1983) (enjoining use of plan assets to protect employer's incumbent management). The legislative analysis of subsection (a)(1)(D) clearly anticipates such an application of the subsection:

> ***127** [Subsection (a)(1)(D)] prohibits the direct or indirect transfer of any plan income or assets to or for the benefit of a party-in-interest. It also prohibits the use of plan income or assets by or for the benefit of any party-in-interest. As in other situations, *this prohibited transaction may occur even though there has not been a transfer of money or property between the plan and a party-in-interest. For example, securities purchases or sales by a plan to manipulate the price of the security to the advantage of a party-in-interest constitutes [sic] a use by or for the benefit of a party-in-interest of any assets of the plan.*
>
> H.R.CONF.REP. NO. 1280, 93rd Cong., 2d Sess. 308, *reprinted in*1974 U.S.CODE CONG. & AD.NEWS 5038, 5089 (emphasis supplied).

In addition, subsection (b)(1) could be applicable to an administrator's investment activities in the context of a corporate control contest, particularly when the administrator is also an officer of the sponsoring corporation or a closely related entity. Subsection (b)(1) requires that a trustee not deal with the assets of the plan "in his *own* interest." (Emphasis supplied.) *See Freund v. Marshall & Ilsley Bank,* 485 F.Supp. 629, 637 (W.D.Wis.1979) (section 406(b) prohibits fiduciary from acting where personal interests may conflict with plan's interest). The question is how broadly "interest" should be read. While it would surely cover trustee interests of a financial nature, one commentator has argued that courts

should not limit the section to financial interests:

The absence of a direct financial interest in the transaction, however, should not preclude the application of this section to officer-trustees, as the prohibited transaction rules are designed to prevent the use of plan assets for any interest, financial or nonfinancial, other than an interest of the plan and its beneficiaries.

Note, *The Duties of Employee Benefit Plan Trustees Under ERISA in Hostile Tender Offers*, 82 COLUM.L.REV. 1692, 1703 n. 51 (1982). In light of ERISA's broad language and protective provisions, we agree that we should read broadly the term "interest" in section 406(b)(1).[FN22] Thus, in a contest for corporate control, plan trustees who are also officers of either the "target" or the "raider" could be seen as having a significant "interest" of their own in the outcome of the contest. Officers of the "target" might well be immediately concerned about holding onto their jobs. Officers of the "raider" might find it in their interest, in terms of maintaining good relations with their superiors, for example, to assist their corporation in its acquisition efforts.

FN22. Where dealings between the fiduciary and the plan are necessary, the exemptions of 29 U.S.C. § 1108 will adequately protect the fiduciary.

C. *ERISA and the Reliable Trust Investments.* Under ERISA sections 404(a), 406(a)(1)(D) and 406(b)(1), where plaintiffs allege that fiduciaries have used plan assets for their own purposes in a corporate control contest, courts must examine closely the circumstances surrounding the alleged use of plan assets. In this case, several factors are relevant in deciding whether the plan administrators acted solely in the interests of the plan beneficiaries. First, the risk of conflicts between the interests of the fiduciaries and beneficiaries is the key warning signal for possible misuse of plan assets. Second, whether fiduciaries with divided loyalties make an intensive and scrupulous investigation of the plan's investment options may be highly probative of the fiduciaries' loyalties. Third, the consistent management of plan assets in congruence with the fiduciaries' personal interests over a substantial period of time in control contests may be probative of whether the fiduciaries have acted solely in the interests of the beneficiaries. This list is by no means exhaustive, but these are the factors applicable here.

On the record before us, we find that the district court clearly erred when it found that the Reliable Trust's investments in Berkeley, OSI and Hickory were made and held solely in the interests of the plan beneficiaries. We find that Dardick's and Zuckerman's investment of the trust's assets in ***128** Berkeley, OSI and Hickory violated ERISA's fiduciary requirements.

With regard to the Berkeley, OSI and Hickory investments, both Dardick and Zuckerman faced the clear risk of conflicting interests. As fiduciaries of the Reliable Trust, their duty was to promote the interests of the trust beneficiaries. Yet their ties to the Engle group and their involvement in the control contests gave them other interests which clearly could diverge from those of the beneficiaries. For example, as the Engle group began to expand its holdings, it benefited by keeping Berkeley, OSI and Hickory stock prices as low as possible in the short run, thereby reducing the cost of its acquisition plans. The Engle group's success in the control contests depended upon the group's ability to control the largest possible block of shares.

The interests of Reliable Trust beneficiaries were markedly different. Their interests were best served by quickly rising stock prices, which often result from corporate control struggles. They certainly had no interest in preventing or delaying price rises. Further, the interests of the beneficiaries required disposing of the stock if it appeared that the investment had no further profit potential. Thus, if fully independent, the persons administering the trust might have wanted to sell the stock before the rest of the Engle group was in a position to cash in its own position. The beneficiaries were interested in the greatest possible return on their investment, regardless of whether their investments aided one side or another in a control contest. Further, independent trust administrators might have sold out earlier (or might never have bought in) if they believed that target management was acting contrary to the best interests of the stockholders.

Thus, as unpaid trust administrators, Dardick and Zuckerman faced responsibilities which could have conflicted sharply with the interests of the Engle group (upon which their income depended) in its control contests. Had a time come when a decision had to be made that would hurt the Reliable Trust and help Engle, or vice-versa, while Engle was effectively providing everyone's paycheck, we think it unrealistic to expect that the decision would not go in Engle's favor.[FN23] To the

extent the Reliable Trust and other entities in the Engle group were stockholders in the same target companies, they shared, of course, an interest in the ultimate maximization of the stock values. In that general sense, the interests were not in actual conflict. However, because the plaintiffs have shown that the trust administrators clearly faced potentially conflicting interests and continued to exercise control over the plan assets in ways that directly benefited the Engle group, grave doubts arise concerning the administrators' loyalty. Under these circumstances, it was virtually impossible for the plan fiduciaries to act with complete loyalty to the Reliable Trust beneficiaries and with an "eye single to the interests of the participants and beneficiaries." *Donovan v. Bierwirth, supra,* 680 F.2d at 271.[FN24]

FN23. When the plaintiffs filed this action in September 1978, the potential conflicts may well have ripened into actual conflicts. The plaintiffs sought immediate distribution of their trust interests, and, as we discuss below in Part V, they may well have been entitled to immediate distribution. When the lawsuit was filed, the Reliable Trust still held its shares of OSI and Hickory, and the control contests for those companies were not over. Yet the trust administrators did not distribute most trust assets until after the control contests had ended. The district court found that the delays were reasonable, and we vacate that finding in Part V. On the record before us, we are reluctant to reverse the district court's finding and hold that the delayed distribution violated ERISA as a matter of law. We leave to the district court on remand the issues whether the fiduciaries' actions in delaying distribution violated the trust instruments or ERISA's standard of loyalty.

FN24. The potential conflicts in the case before us seem, on the surface, at least, less severe than the one faced by the trust administrators in *Donovan v. Bierwirth,* where the administrators' positions in target management, and their presumed concern for their own jobs, might have been influences strongly adverse to the trust's interests as a stockholder. Nonetheless, the potential conflicts in this case were substantial enough to create the risk of misuse of plan assets.

***129** Because of the other factors present in this case, we need not decide whether the potential conflicts alone amounted to ERISA violations. Where they faced these clearly conflicting loyalties, Dardick and Zuckerman undertook no genuinely independent investigation of the trust's investment options. At the very least they should have realized that their ties to the Engle group and their interests in the control contests cast serious doubt on their ability to act solely in the interests of the beneficiaries. Yet before the trust purchased the stocks and throughout the several control contests, Dardick and Zuckerman failed to seek independent advice which might have clarified where the interests of the beneficiaries lay.

Defendants contend that the trust's Berkeley purchases were prudent investments made upon the advice of the professional investment advisor, Charles Newbill. The reliance on Newbill's advice does not alter our conclusion that the investments were not made for the exclusive purpose of providing benefits to plan beneficiaries. On the contrary, in light of Newbill's ties to the entire Engle group, *see supra* Part I-A, his blessing of the trust's investments only adds support to the inference that the trust purchases were part of the Engle group's investment and acquisition program. First, at the time Newbill proposed the Berkeley investments to Dardick, Newbill's only paying client was Libco. The bill Newbill submitted to the Reliable Trust for the advice was prepared nine months after the purchases and three months after this lawsuit was filed. Newbill apparently made his recommendations in several conversations with Dardick during early 1978 and in several brief memoranda dated a few days before the trust made its purchases. *See* Defendants' Exhibits ZZ and AAA. Dardick and Zuckerman clearly knew of Newbill's involvement with Engle and Libco, and they were aware of Engle's and Libco's interest in the three companies. If Dardick and Zuckerman had been acting independently, we do not see how they could have failed to make their own investigation or to seek the advice of someone not involved in the Engle group's acquisition efforts.[FN25]

FN25. Defendants argue further that the Berkeley purchases, as well as those of OSI and Hickory, were prudent and made to diversify the trust's assets. To support this claim, defendants point to the testimony of Lee Meyer, a Harris Bank officer, who testified that the Harris Bank had also purchased Berkeley shares in the Special Capital Fund it managed for many employee benefit plans. Defendants' Brief at 19, 38. However, Meyer also testified that the

> Special Capital Fund was "a highly speculative fund, high risk fund," and a "go-go fund." Transcript at 613, 620. He testified that the bank never put more than 5% of any single trust's assets in the Special Capital Fund because the investments were high risk. Transcript at 613. The narrow issue of prudence is not precisely before us on this appeal. However, the speculative nature of the Reliable Trust's investments and the fact that the investment in Berkeley apparently appreciated primarily through the use of litigation as an economic weapon indicate whether the plan administrators acted with unswerving loyalty to the trust beneficiaries.

Additionally, defendants point out that the Reliable Trust's investments had all been held in the form of fixed income securities until March 1978, and that they were required to diversify these holdings. See 29 U.S.C. § 1104(a)(1)(C). We do not question the need for diversification; in the abstract, it was entirely proper for the trust to purchase common stocks. However, the problem in this case is the particular choice of stocks in light of the other defendant's holdings in Berkeley, OSI and Hickory, and in light of the administrators' own interests, previously discussed, in these companies. A general need or desire for diversification cannot serve to justify the choice of the stocks purchased in this case.

Thus it is clear that the Reliable Trust investments in Berkeley, OSI and Hickory were made by administrators who faced conflicting loyalties and who made no effort to obtain independent advice regarding these investments and the interests of the trust beneficiaries. When we also examine the timing of the trust's investment decisions and their relationship to the actions of other members of the Engle group, it is clear that the trust's investments were not made with an "eye single" to the interests of the participants and beneficiaries. *Donovan v. Bierwirth, supra,* 680 F.2d at 271. Instead, the trust investments were made at least in part to enhance the Engle group's position in the several control contests.

***130** The timing of the Reliable Trust purchases of Berkeley stock in relation to other actions of the Engle group shows that the trust assets were not used exclusively to further the interests of the trust beneficiaries. In late February 1978, Engle learned of the proposed deal between Berkeley management and the Cooper group trying to take over the company. At that time, Engle believed that the proposed deal would work to the disadvantage of minority shareholders such as himself and GSC. Although they faced the danger of being "locked-in" as minority shareholders under hostile management, Engle and GSC purchased an additional 11,200 shares between February 27th and March 10th, increasing the Engle group's Berkeley holdings from 3.5% to 4.0% by March 10th. Then, on March 22, 1978, letters were sent on GSC letterhead to the outside directors of Berkeley protesting the proposed Berkeley-Cooper deal. The letters were sent in Engle's name, but Dardick (who was, of course, at the same time the Reliable Trust administrator) prepared the letters and signed them for Engle. On April 7, 1978, Sierra, Engle and GSC filed suit against Berkeley and Cooper in the federal district court for the Northern District of Illinois. The complaint sought to enjoin the proposed deal, and Dardick prepared and signed the complaint. Thus, as attorney for Engle, Sierra and GSC, Dardick was arguing that Berkeley management was acting against the interests of minority shareholders, and he was suing management to stop the Berkeley-Cooper deal.

Meanwhile, between March 17th and March 31st, as administrators of the Reliable Trust, Dardick and Zuckerman were investing over $71,000 of the trust's assets in Berkeley stock. Under their direction, therefore, the Reliable Trust was becoming one of those minority shareholders against whose interests the Berkeley management was supposed to be acting. The Reliable Trust purchases of Berkeley stock increased the Engle group's block of Berkeley shares from 4.0% to 4.65% between March 17 and March 31, 1978. The suit by Engle, Sierra and GSC was settled in June 1978 by having Cooper Laboratories buy at a substantial premium the Berkeley shares owned by the Engle group. The Reliable Trust was not a party to the lawsuit, yet its Berkeley shares were also purchased as part of the settlement.[FN26]

> FN26. Of course, Dardick could also have been criticized if the trust shares had *not* been included in the settlement, for then the trust would not have received the control premium offered by Cooper. The dilemma stems from the fact that Dardick owed a fiduciary's duty of loyalty both to the trust and to the other members of the Engle group whose interests potentially diverged from those of the trust.

We believe that undisputed facts in the record show that the Reliable Trust investments in Berkeley were made at least in part for the benefit of other members of

the Engle group in their effort to acquire a substantial block of Berkeley shares. Engle's response to the Berkeley-Cooper deal was to gain control of more Berkeley shares and to sue Berkeley management to force a favorable settlement. We can see no reason for including the Reliable Trust shares in the ultimate settlement unless the trust's shares were in fact subject to the Engle group's control in the contest for control of Berkeley. One reason for the trust purchases of Berkeley stock was to increase the Engle group's control of Berkeley and, from the perspective of the trust, to gamble on the outcome of the expected litigation and control contest. As we noted above in Part II, the fact that the gamble paid off for the trust as well as for the rest of the Engle group is no defense in this action for breach of fiduciary duties.

The Reliable Trust investments in OSI stock show a similar pattern. The trust made its investments in OSI very early in the struggle for control of OSI. Before Telco began purchasing OSI stock on April 17, 1978, GSC, Engle and the Reliable Trust owned a total of 24,100 shares, or 1.67% of OSI. The trust owned 12,500 of those shares. Beginning on April 17th, Telco and later Telvest purchased OSI steadily, and the group's holdings grew to 6.2% by the end of May 1978, 9.7% by the end of July, 16% by the end of October, and 21.73% on May 4, 1979. Throughout the period of the Telco and Telvest purchases, the Engle ***131** group fought for control of OSI through litigation, two tender offers and a proxy fight. The Reliable Trust held its OSI shares during this time and ultimately sold them for an enormous profit when the Brown Group tendered $15.00 per share as a "white knight" protecting OSI management.

Dardick acted as attorney for the Engle group in the proxy fight, the tender offers and the ancillary litigation. On behalf of the Engle group he was sharply critical of OSI management and the company's profitability. His efforts were aimed at forcing OSI management to yield control or to purchase the Engle group's shares at a premium. At the same time, Dardick directly controlled the Reliable Trust's investments in OSI, and he directed the Harris Bank to vote the trust's shares in the proxy fight in favor of the Engle group's candidates for the board of directors.

Like the Reliable Trust's Berkeley investments, the OSI investments were made, held and used while the Engle group was engaged in a struggle for corporate control against the incumbent management. The trust administrators and the Reliable Manufacturing board of directors were all deeply involved in those struggles. They had significant interests of their own at stake in the outcome of the struggle. Clearly there was no one who had discretionary authority over the trust investments and who was disinterested in the struggles for corporate control. And throughout the control struggle lasting over a year, the Reliable Trust held its OSI shares and used them in accord with the Engle group's best interests.

The Hickory investments display the same pattern, although Hickory management decided not to resist the Engle group's efforts to gain control of the company. Again, the administrators faced conflicting loyalties, at least until it became clear that the Engle group would be successful in its acquisition efforts. The Engle group wanted to keep the stock price down in the short run, while an independent trust would probably have been interested in quickly rising stock prices. Again, there was no effort to obtain independent advice on the soundness of the trust's purchase and retention of Hickory shares. Throughout the long period during which the Engle group established its position in Hickory, the trust held its shares. Then, after it was clear that the Engle group would succeed, the trust sold its shares at a low point in the market for a net profit of 4%, including a loss on one-third of the shares it purchased. Under these circumstances, we conclude that the district court erred when it found that the defendants fulfilled their duties under ERISA.[FN27] Dardick and Zuckerman violated their duty of loyalty by investing the trust's assets in Hickory because they were not acting solely in the interests of the beneficiaries.[FN28]

> FN27. The plaintiffs claim that defendants profited from their Hickory investments primarily through the use of "equity accounting," whereby as investors with "substantial influence" over Hickory, the defendants were able to include their share of Hickory's earnings in their own balance sheets. The district court found that the Reliable Trust's Hickory shares "played no part in the decision by, or ability of, Telco to use the equity method of accounting" with respect to its Hickory investments. Finding of Fact No. 15. That finding, which is not clearly erroneous, is relevant in determining whether and how the defendants profited from the trust's investments in Hickory. However, our conclusion that the investments violated ERISA's standard of loyalty does not depend upon the use of equity